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SUBJECT: LAN CHILE - OPEN SKIES POSTERCHILD

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1. (SBU) SUMMARY. U.S. Department of Transportation officials facilitated a conference call between senior executives from the Chilean airline, Lan Chile; U.S. State Department and DoT officials; and South Africa,s Director of Air Transport Regulation and chief aviation negotiator Godfrey Selepe. The Lan Chile officials compared Chile to South Africa and attributed much of their success and Chile,s economic growth to the Open Skies agreement signed with the United States in 1997. The officials felt that a step-by-step liberalization of the aviation regime would not have brought Chile the same economic benefits as an Open Skies agreement. In addition, they said that Open Skies provides a more flexible business environment which especially benefits smaller firms. Selepe said that President Mbeki,s policy has been one of managed liberalization. In this context, he said that South Africa,s aviation policy is not necessarily pro-Open Skies, but doesn,t prohibit it either. He added that South Africa,s aviation policy must consider the administration,s main priorities of alleviating poverty and creating jobs. Selepe said that he had hoped to remove some restrictions during the last round of negotiations in 2000 and looks forward to following up on this angle during the current negotiations. END SUMMARY.

2. (U) U.S. Department of Transportation (DoT) Deputy Assistant Secretary for Aviation and International Affairs Susan McDermott facilitated a January conference call between senior executives from the Chilean airline, Lan Chile; U.S. State Department and DoT officials; and South Africa,s Director of Air Transport Regulation and chief aviation negotiator Godfrey Selepe. Lan Chile executives included President and CEO Luis Ernesto Videla, General Counsel Juan Carlos Mencia, Director of Commercial Planning Jorge Grainger, and Director of Commercial Analysis and Development Raquel Galarza. South Africa,s Minister of Transport Jeffrey Radebe and South African Airways officials were unable to participate in the call.

SIMILARITIES BETWEEN CHILE AND SA

3. (U) Videla began by comparing Chile to South Africa. He described Chile as a small, liberal economy distantly removed from the world,s most important economic regions. He said that in the 1990s Chile was looking to grow its economy and viewed its relationship with the United States as a means to accomplish that. Videla admitted some fear at the thought of competing head-to-head with the larger U.S. airlines. However, the opportunity to gain greater access to the larger U.S. market outweighed Lan,s reservations and they supported the move to an Open Skies (OS) agreement with the United States in 1997. Raquel Galarza said that Open Skies is important to countries like Chile and South Africa because it provides the flexibility that is necessary for smaller companies to rapidly change their operational plan according to market conditions.

PROOF IS IN THE PUDDING

4. (U) Jorge Grainger commented that Latin American countries with OS agreements produce stronger airlines. He pointed out that Chile has over 100 frequencies with Argentina, 59 with Brazil, and 24 with Peru. On the other hand, there are just 14 frequencies between Brazil and Peru and 24 between Argentina and Peru. Grainger,s point was that despite restrictive agreements with its neighbors, Chile enjoyed a net advantage in frequencies because Chile is liberalizing its economy more rapidly.

5. (U) Grainger continued that in the seven years since Chile and the United States signed an OS agreement, Lan Chile has enjoyed the following successes:

- Passenger load has increased 1.6 times
- Cargo load has increased 1.7 times
- Direct flights to U.S. cities increased from 3 to 6
- Increased codeshare services have added 29 U.S. cities and 7 Chilean routes to Lan Chile,s service.
- Lan Chile,s frecuencies have increased 60 percent
- Lan Chile has 70 percent more seats
- U.S./Chilean carriers have increased in direct flight market share from 86 to 98 percent

16. (U) Videla added that removing restrictions on air transport has been directly related to the successful development of Chile,s broader economy. In 1990, exports by air were almost zero. Today, Chile exports more than 120 tons of goods per year on 300 freighters and Lan Chile has become the most important cargo company between the U.S. and South America with the liberalization of 7th freedom rights under Open Skies. Grainger added that agreeing to a full Open Skies agreement has helped Chile develop its telecommunications and IT industries with an influx of reservation and call centers.

17. (U) Juan Carlos Mencio said that OS has strengthened relations between the two countries and ushered in an era of greater cooperation on transportation and aviation matters. The agreement allowed the United States to offer training to Chilean officials that was not available under the old aviation regime.

CAN OPEN SKIES BE PHASED IN?

18. (U) Videla was doubtful when asked whether Chile would have benefited as much from a step-by-step liberalization of its aviation industry. He said Lan Chile feared that an incremental approach may have resulted in something less than Open Skies. Galarza said that Open Skies creates a climate where companies can determine how they will respond to rapidly changing market conditions as opposed to an industry controlled by government-imposed conditions. Non-OS regimes inhibit the ability of companies to exploit changing circumstances and the bureaucratic process moves too slowly to meet the demands of industry.

SELEPE,S RESPONSE

19. (SBU) Selepe described the conference call as more operational than regulatory in nature. He regretted that South African Airways representatives were unable to participate in the call and said that they missed a lot.8 Selepe said that South Africa is still a young and inexperienced democracy. Unlike Chile, he explained that South Africa is not yet a completely liberal regime and President Mbeki,s policy has been one of managed liberalization. In this context, he said that South Africa,s aviation policy is not necessarily pro-Open Skies, but doesn,t prohibit it either. He added that South Africa,s aviation policy must consider the administration,s main priorities of alleviating poverty and creating jobs.

10. (SBU) Selepe pointed out that all stakeholders in South Africa (i.e., tourism, SAA, international airlines operating in South Africa, etc.) would participate in the Open Skies discussion, but that no one specific party exercised decisive influence on the outcome. At the end of the day, South Africa,s Department of Transport would decide whether or not to adopt an Open Skies agreement with the United States. Selepe said that he feels South Africa enjoys good relations with the United States via the International Civil Aviation Organization (ICAO). He said that while the current bilateral agreement with the United States has some restrictions, it is certainly not the most protectionist. Selepe said that he had hoped to remove some restrictions during the last round of negotiations in 2000 and looks forward to following up on this angle during the current negotiations.

FRAZER